

No. 13,765

IN THE

United States Court of Appeals
For the Ninth Circuit

G. L. THOMPSON, as Trustee in Bankruptcy of the Union Lead Mining and Smelter Company, bankrupt,

Appellant,

VS.

R. H. DACHNER,

Appellee.

Appeal from the United States District Court, Northern
District of California, Southern Division.

BRIEF FOR APPELLANT.

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FILED

NOV 20 1953

PAUL P. O'BRIEN
CLERK

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JURISDICTIONAL STATEMENT.

A petition for ancillary administration in bankruptcy was filed in the United States District Court for the Northern District of California, Southern Division, pursuant to Section 20, Subdivision 2A(20) of the Bankruptcy Act, 11 U.S.C. 43. Said petition was referred to the Referee in Bankruptcy under Section 38(6) of the Bankruptcy Act, 11 U.S.C. 66.

The Referee in Bankruptcy issued a Rule to Show Cause for a Turn Over Order. Following hearing on

Rule to Show Cause, a Petition to Review was filed in the United States District Court for the Northern District of California, Southern Division, pursuant to Section 39(c) of the Bankruptcy Act, 11 U.S.C. 67.

Following affirmance of the decision of the Referee, this appeal was commenced in the Court of Appeals for the Ninth Circuit pursuant to Section 24, Subdivision (a) of the Bankruptcy Act, 11 U.S.C. 47.

STATEMENT OF THE CASE.

The factual situation which gives rise to the appeal before this Court is briefly as follows: On June 16, 1947, the Second Judicial District Court of the State of Nevada entered a judgment in favor of R. H. Dachner (R.T. 112), the appellee here, against the Union Lead Mining and Smelter Company, the appellant here. An appeal was taken from this judgment to the Nevada Supreme Court in July, 1947. While this appeal was pending, Dachner, on November 20, 1947, on the basis of his judgment successfully levied execution on the bank account of Union Lead Mining and Smelter Company, obtaining thereby the sum of twenty-six thousand two hundred sixty-six and 81/100 (\$26,266.81) dollars. (R.T. 115.) Thereafter, Union Lead Mining and Smelter Company, on February 7, 1948, filed a voluntary petition in bankruptcy and was adjudicated a bankrupt on February 9, 1948. (R.T. 27.) On June 25, 1948, the Nevada

Supreme Court reversed the judgment previously entered on behalf of Dachner and remanded the cause for a new trial as to all the issues of the case. (R.T. 117.) Subsequently, a judgment was again entered in favor of Dachner, which judgment was affirmed by the Supreme Court of Nevada. The parties to the proceedings in the Nevada courts were: R. H. Dachner, doing business under the firm name and style of Pacific Machinery and Engineering Company, Plaintiff, versus Union Lead Mining and Smelter Co., a Nevada corporation, Defendant. (R.T. 112.) On the 5th day of June, 1951, a Petition for Ancillary Administration in Bankruptcy was filed in the United States District Court, by G. L. Thompson as Trustee in Bankruptcy of Union Lead Mining and Smelter Co., Bankrupt. (R.T. 3.) Subsequent to this petition, an Order was entered by United States District Court that the matter be referred to the Referee in Bankruptcy and that R. H. Dachner show cause why he should not turn over to the trustee the sum of twenty-six thousand two hundred sixty-six and 81/100 (\$26,266.81) dollars. (R.T. 10.) The Referee in Bankruptcy found that the Court was without jurisdiction to proceed upon the petition filed by the Trustee in the above entitled District Court; that the petition be dismissed; and that the Order to Show Cause be discharged. (R.T. 38.) The Order of the Referee was confirmed by the District Court. (R.T. 49.)

QUESTION RAISED ON APPEAL.

The question raised on this appeal is:

Did the District Court have summary jurisdiction over the funds in the possession of R. H. Dachner so as to require the issuance of a Turn Over Order?

SPECIFICATION OF ERRORS.

The appellant assigns as error the following acts and omissions of the Referee in Bankruptcy and the District Court.

1. The Referee erred in failing to find that no appearance was made by the Trustee in any of the proceedings before the Courts of Nevada and that there was no order issued out of the Federal Court directing such appearance and that there was no order entered in either the bankruptcy or reorganization proceedings allowing the Dachner claim to be litigated in the State Courts.

2. The Referee erred in finding that R. H. Dachner did not have under his control any of the assets of the bankrupt subsequent to February 7, 1948; and in finding that no part of the assets of the bankrupt came into the actual or constructive possession of R. H. Dachner after the filing of the bankruptcy petition on February 7, 1948; and in failing to find that upon the reversal of the State Court judgment on June 25, 1948, upon which judgment execution had previously been levied by the said R. H. Dachner on November 20, 1947, in the sum of twenty-six thou-

sand two hundred sixty-six and 81/100 (\$26,266.81) dollars, that said sum of money instantly became an asset of the bankrupt and the said R. H. Dachner held it as constructive trustee.

3. The Referee erred in his Conclusion of Law No. 1 that said Court was without jurisdiction to proceed.

4. The Referee erred in his Conclusions of Law No. 2 and No. 3 to the effect that the petition should be dismissed and that the Order to Show Cause based thereon should be discharged.

5. The Referee erred by holding in effect that the State Court had the power, during the bankruptcy proceeding, to diminish the assets of the bankrupt estate by determining therein that a compromise had been effected by certain officers of the debtor, when the action was *in personam* and no appearance had been entered by the Trustee in Bankruptcy in the State Court proceedings, nor had the Trustee been directed to enter an appearance, nor had there been any order directing that the claim might be litigated in the State Court.

6. The Referee erred in failing to find that Dachner had in his possession the sum of twenty-six thousand two hundred sixty-six and 81/100 (\$26,266.81) dollars, the asset of the bankrupt, and in failing to overrule the objection to summary jurisdiction.

7. The honorable District Court erred in confirming the Order of the Referee in Bankruptcy entered on March 12, 1952.

ARGUMENT.**I.**

**THE CONCLUSION OF THE DISTRICT COURT AND THE REF-
EREE THAT THE COURT LACKED SUMMARY JURISDICTION
TO PROCEED ON THE RULE TO SHOW CAUSE WAS ER-
RONEOUS.**

The District Court had summary jurisdiction to issue a turn over order where the funds passed to the constructive possession of the Trustee in Bankruptcy for the Union Lead Mining and Smelter Company, in which case the claim of R. H. Dachner would not be adverse and substantial.

That the property passed to the constructive possession of the Trustee in Bankruptcy for Union Lead Mining and Smelter Company, and that thereafter R. H. Dachner held said property as a constructive trustee, is clear from the following legal principles and authorities.

1.

When a judgment is reversed and remanded for a new trial, the parties are returned to the status existing prior to the judgment.

“When a judgment is reversed it becomes, insofar as the parties to the action are concerned, the same as if it had never been rendered and the foundation of any proceeding which may have been had by way of execution thereunder is taken away. *Cowdery v. London & San Francisco Bank*, 139 Cal. 398, 73 P. 196, 96 Am.St.Rep. 115; *Bogga v. North American Bond, etc., Co. (Cal. Sup.)* 58 P. 2d 918; *Levy v. Drew*, 4 Cal. 2d 456 at page

459, 50 P. 2d 435; Caroy v. Dowdell, 131 Cal. 499, 63 P. 2d 780.”

First Trust Joint Stock Land Bank of Chicago v. Meredith, 64 P. 2d 977.

“When the order of the Supreme Court * * * was made, reversing the judgment of the court below, that judgment was forthwith vacated, *and until action was taken by the court below in pursuance of the mandate, to enter another judgment in accordance with the opinion of the Supreme Court, there was no judgment in existence in the case.*” (Italics ours.)

Cowdery v. London & San Francisco Bank, 139 Cal. 398, 73 P. 196.

In applying this principle to the facts of this case, it is apparent that when the judgment upon which the execution was issued was reversed by the Supreme Court of Nevada, on June 25, 1948, the foundation of the execution was swept away and the parties stood in the same position as though no judgment had been rendered. Consequently, as of this time, Dachner had in his possession funds of Union Lead Mining and Smelter Company. Since Union Lead Mining and Smelter Company was a bankrupt at that time, constructive possession of the funds passed by operation of law to the Bankruptcy Court.

2.

A party who has levied execution on a judgment that is subsequently reversed and remanded for a new trial, has the duty to make restitution to the other party. If restitution is not made he holds the property as a constructive trustee.

The Restatement of the Law of Restitution, Section 74, provides:

“Judgments Subsequently Reversed.

A person who has conferred a benefit upon another in compliance with a judgment, or whose property has been taken thereunder, is entitled to restitution if the judgment is reversed or set aside unless restitution would be inequitable or the parties contract that payment is to be final. If the judgment is modified there is a right to restitution or the excess.”

Comment:

“* * * the fact that the judgment was merely set aside and that no final judgment was entered for the payor does not prevent restitution. If the Appellate Court vacates a judgment and orders a new trial, a person who has satisfied the judgment vacated is entitled to restitution. See Illustration 3.”

“3. A obtained a judgment against B for a thousand dollars. B paid the judgment. On appeal the judgment is set aside and a new trial ordered. In the absence of other facts, B is entitled to restitution from A.”

The view of the Restatement is supported by the cases. See:

Ex parte Walter Bros., 89 Ala. 237, 7 So. 400,
18 Am. St. Reports 103;

Levy v. Drew, 50 P. 2d 435, 101 A.L.R. 1147.

In *Levy v. Drew* (supra) the Supreme Court of the State of California set forth this doctrine as follows:

“It is well settled in California that when a judgment is reversed on appeal the appellant is entitled to restitution of all things taken from him under the judgment. After reversal, the respondent stands in the position of a trustee of appellant of the property obtained under the judgment. Restitution may be sought in the same or in an independent action.”

“We therefore conclude that defendant had no right to retain the money collected under the execution after the judgment upon which it was issued had been vacated.

“There remains for determination the question of defendant’s right to offset his claim for services rendered against the claim of the plaintiff for restitution of the money unlawfully held by defendant.

“The rule is consistently applied in the federal courts that when a debtor, prior to bankruptcy, voluntarily places in the hands of his creditor assets for the particular purpose of extinguishing a debt, and bankruptcy occurs, the creditor can offset his demand against the claim of the trustee in bankruptcy for a return of the assets to the bankrupt estate. It is equally well settled that the unauthorized possession of funds of the bankrupt can give the creditor no right to apply them to the payment of his own claim to the prejudice of the rights of other creditors. *Emerson v. Fisher* (C.C.A.) 246 F. 642; *Lehigh Valley Coal Sales Co. v. Maguire* (C.C.A.) 251 F. 581; *Alvord v.*

Ryan (C.C.A.) 212 F. 83; In re Interborough Consol. Corporation (C.C.A.) 288 F. 334, 32 A.L.R. 932; Parker State Bank v. Pennington (C.C.A.) 9 F. (2d) 116; Cook County Nat. v. United States, 107 U.S. 445, 2 S. Ct. 561, 27 L. Ed. 537; In re Gans & Klein (D.C.) 14 F. (2d) 116; Hanover Nat. Bank v. Suddath, 215 U.S. 122, 30 S. Ct. 63, 54 L. Ed. 120.

“In the instant case the money was not voluntarily paid to defendant by the corporation, but was forcibly seized by the levy of an execution, nor was it voluntarily handed over to be applied on the particular debt owed to defendant. *When his judgment was vacated, defendant’s possession of the money became illegal and he should have restored it to his debtor. It follows that defendant cannot offset the amount of his claim against the suit of the trustee in bankruptcy for the money which he unlawfully retained but must restore it and take his place among the general creditors of the bankrupt estate.*” (Italics ours.)

It stands without question that on June 25, 1948, on which date the Supreme Court of Nevada reversed and remanded the judgment upon which Dachner had seized the funds of the bankrupt, that thereafter Dachner’s possession of those funds became illegal. He was obligated, legally as well as morally, to restore the funds to the bankrupt and take his position with other general creditors of the bankrupt estate.

3.

Funds held by a constructive trustee are held without right or claim.

The Supreme Court of California, in *Bainbridge et al. v. Stoner et al.*, 106 P. 2d 423, in discussing the definition and underlying theory of constructive trusts, stated:

“The theory of a constructive trust was adopted by equity as a remedy to compel one to restore property to which he is not justly entitled, to another. The person having acquired it through fraud, undue influence, breach of trust, or in any other improper manner and he is usually personally liable in damages for his acts. But the one whose property has been taken from him is not relegated to a personal claim against the wrongdoer, which might have to be shared with other creditors; he is given the right to a restoration of the property itself.”

Since the funds of the bankrupt were illegally held by Dachner, after the reversal of the judgment by which he obtained possession of them, he became a constructive trustee of the funds for the bankrupt. The trustee for the bankrupt was, therefore, immediately vested with the right and title to the funds and he could not be divested of his right to the funds by any *in personam* proceedings between Dachner and Union Lead Mining and Smelter Company, to which he was not a party. Therefore, the subsequent *in personam* proceedings in the Nevada Courts between Dachner and Union Lead Mining and Smelter Company would not divest the Trustee

in Bankruptcy for Union Lead Mining and Smelter Company of his constructive possession of said funds in the absence of his appearance in such subsequent proceedings.

In *Rhodes v. Elliston*, 29 F. 2d 737, claimant obtained a judgment in the State Court against the bankrupt for conversion of certain cotton bales. He subsequently offered to file a copy of this judgment as proof of claim against the bankrupt which offer was rejected even though suit had been commenced prior to bankruptcy and the trustee had been given notice of the action. On an appeal from this decision, the Court held:

“The judgment was a personal one against the bankrupt. It was not binding upon the bankrupt estate because the trustee was not made a party defendant. Under sec. 11(d) of the Bankruptcy Act, the exclusive power to order a trustee to defend a suit in a state court is vested in the bankruptcy court. It therefore was not error to refuse to accept the judgment of the state court as conclusive proof of the claim in question.”

Thus the subsequent proceedings in the Nevada Court could affect only the perfection of Dachner's claim and the right to take his position as a general creditor of the bankrupt upon the basis of judgment. It could not establish his right to any specific funds whether in his possession as constructive trustee or otherwise as to the Bankruptcy Court. See 10 Collier, Bankruptcy, page 964, wherein that proposition is set forth as follows:

“Where a petition has been filed against an alleged bankrupt another court has no right to seize, attach, fix a lien, or otherwise affect the bankrupt’s property by virtue of proceedings begun thereafter, unless with the consent of the bankruptcy court, regardless of whether or not actual possession has been taken by the bankruptcy court’s officers.”

CONCLUSION.

In view of the foregoing, it is respectfully urged that the judgment of the honorable District Court should be reversed and the matter be returned to the honorable District Court for issuance of a Turn-Over Order.

Dated, San Francisco, California,
November 13, 1953.

Respectfully submitted,

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